RICHARD RUSSELL'S DOW THEORY LETTERS INCORPORATED

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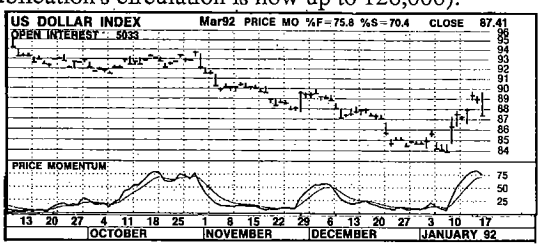
Jan. 22, 1992 **LETTER 1087**

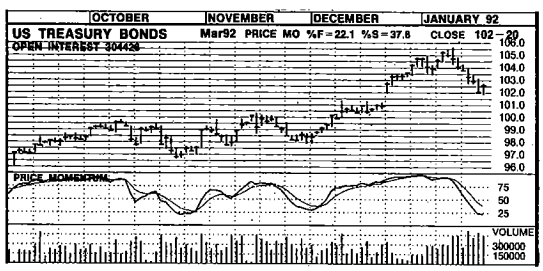
Jan. 10 DJIA 3199.46; PTI 3435; A-D Ratio -9.40
Jan. 17 DJIA 3264.98; PTI 3445; A-D Ratio -8.87
Dow Yield: 2.83%; Dow P/E: 32.4; DowPow: 208
Dow 200-day MA: 2986; Dow 30-day MA: 3050
Dow Times Book Value: 2.45; PTI 89-day MA: 3403
Percentage of Undervalued Blue-chips: 8%

THE ULTIMATE IRONY? It's January 1, 1993. Saddam Hussein is still in power -- and his nemesis, George Bush, is history. Mmm, it's just a thought.

CHARTS: I want to start this Letter a little differently -- with a few critical charts. First, the **dollar** -- gad, has it put in a bottom, has it finally reversed to the upside, is this the turn? It sure looks like it. Ironically, everyone is now on the German bond bandwagon (*WSJ* - Jan. 14), and, of course, the one thing you don't want to see if you're loaded with German government bonds (or any kind of foreign securities, for that matter) -- is a humongous dollar rally. Nevertheless, it's looking increasingly as though the dollar wants to head north. But why? One theory (and it's only a theory): later in '92 the US economy may be coming out of the recession while conversely Europe may be sinking deeper into recession. If that happens, the dollar could be the hero of 1992 (charts courtesy of *Investor's Business Daily* -- by the way, this fine publication's circulation is now up to 126,000).



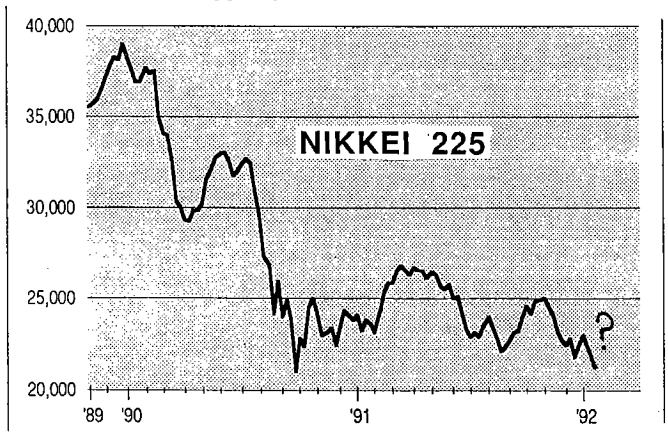
However, if the stock market is correct, if better times are coming for the economy, then it is also probable that **interest rates** have bottomed and are now in the process of creeping higher. Massive US deficits could also put upward pressure on interest rates. We'll watch the **long bonds** (this is the area that the Fed cannot manipulate). This chart shows the Treasury bond futures looking suspiciously toppy. Also, note that the Utility Average (page 1 chart) has been heading down, and Utilities are extremely sensitive to forthcoming changes in interest rates.



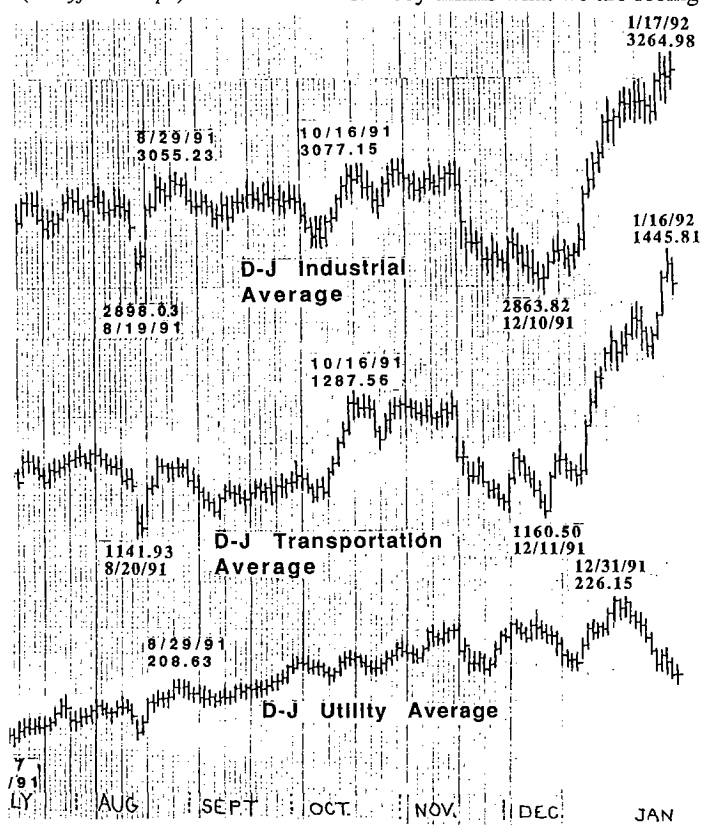
I feel the **Japanese situation** is moving towards the critical stage. Japan led all the world's markets on the upside from 1949 on, and I'm wondering whether Japan won't continue to be the leader during the '90s.

In Japan the favorite collateral by far is land. Roughly 40% of all formal bank loans in Japan are backed by land values, and many more are backed informally by land. Thus, the continued weakness in Japanese land prices constitutes a major threat to their economy. As property prices decline (and they are doing just that), the collateral behind bank loans declines in value.

The big question: Can Japan's Nikkei stock average hold above the critical 20,000 level? If it can't --there's going to be trouble -- and I mean trouble around the world. Below 20,000 on the Nikkei and many of Japan's banks will be severely squeezed, since the Japanese banks count stock assets and profits as part of their capital. Last week the Nikkei broke below 22,000. I have my eyes on the Nikkei, and I suggest you do the same.



THE PICTURE: Last week's stock market surge took it to new record highs, and now the analysts and economists are moving to rationalize what Wall Street has wrought. Is there a good fundamental case for the bulls? Leading economist Richard Hoey (*Dreyfus Corp.*) believes there is. Hoey thinks what we are seeing



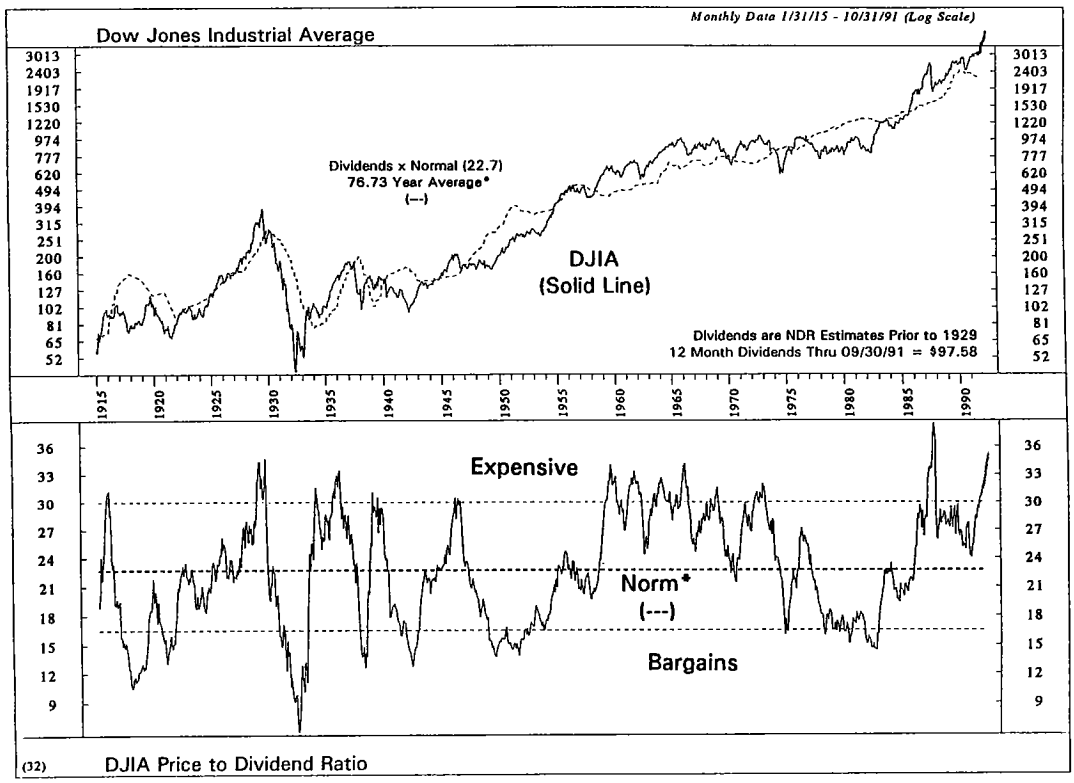
now is an orderly de-leveraging of the economy rather than a disorderly de-leveraging (the latter is the kind that could trigger a depression). Hoey bases his opinion on certain indications such as stock prices rallying, bank stocks rising, and the spread between junk bonds and Treasuries narrowing. With the exception of commercial real estate, which is mired in depression, the above listed symptoms, states Hoey, are bullish.

Hoey believes that when the real GNP for the third quarter is announced (in late October), the "October economic surprise" will be real GNP growth of 4% or more. "We would expect the US economy to be the strongest major economy in the world in the second half of 1992," opines Hoey.

So there it is, the bulls' scenario. And the Russell comment is this: "Let's drop all preconceived notions. Let's keep an open mind. Everything Hoey says could come to pass. But there's a problem. The problem is that this market has already positioned itself so that the bullish scenario MUST come to pass. I say this because the stock market is already selling at one of its priciest levels of this century. So it's not a case of whether the economy is going to turn up, it's a case of -- the economy BETTER turn up."

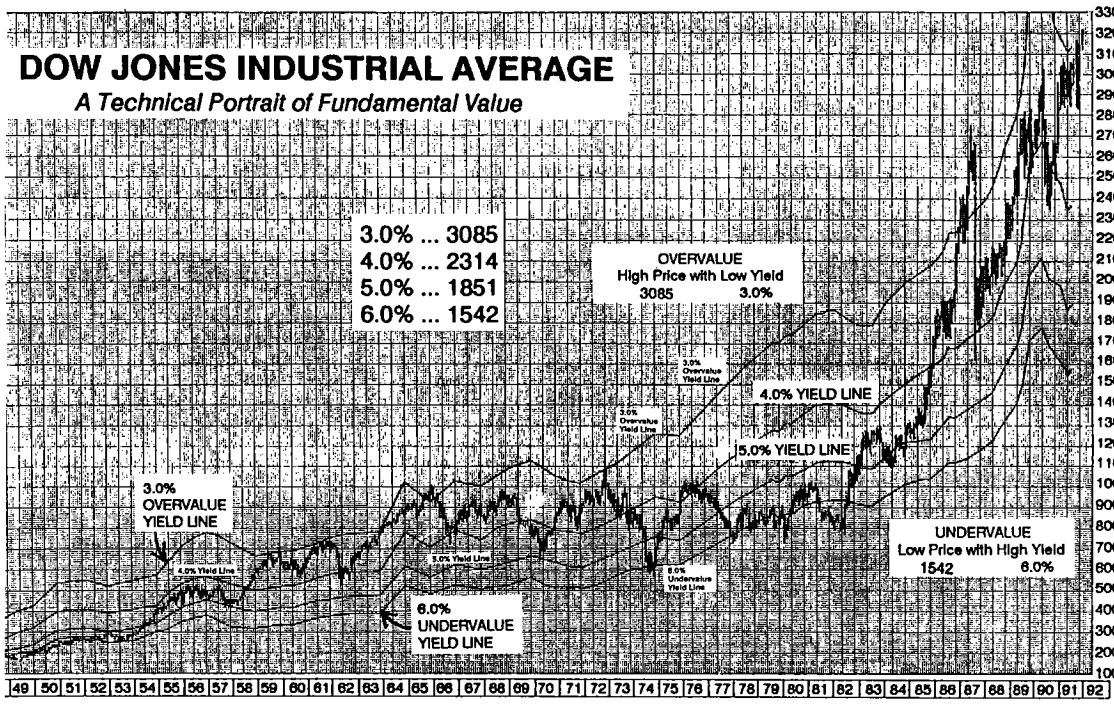
THE MARKET: Recent market action was explosive, but also quite unusual. The Dow struck a low on December 11, then turned up. The rise turned into a power-surge. The Dow was up 11 trading days in a row with the series ending on January 5. Moreover, the market (NYSE) produced a thousand or more advances in each of the seven days from December 20th through the 31st. That's impressive action.

As for breadth, the low day for the advance-decline ratio was recorded on December 11 at -12.26. By January 17 the A-D ratio had rallied to -8.87, a gain of 3.39 points. Was it a "buying stampede?" Not yet. Not by my definition (and I've used this definition for the last 25 years). A buying stampede is a rise of five points or more on the A-D ratio, uninterrupted by so much as a one point correction.



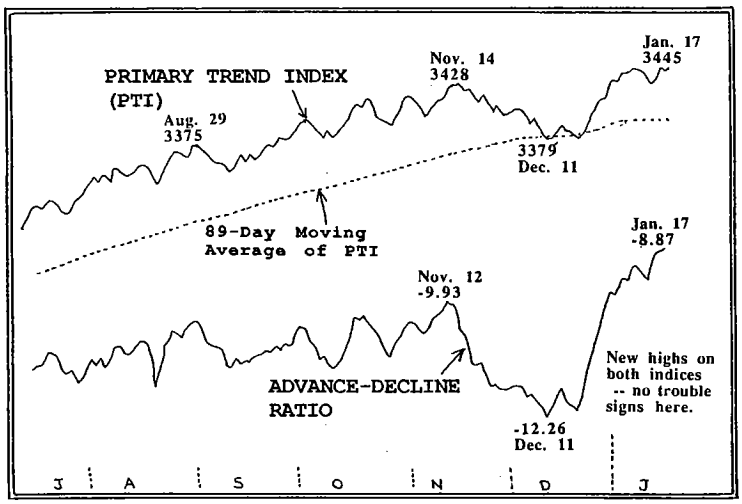
So what we experienced is something I'd call an upside explosion, but it does not yet fit the definition of a "buying stampede." To do that, we need considerably more uninterrupted upside breadth action.

From a Dow Theory standpoint based on valuation and yield, the stock market is now at a critical and fascinating juncture, and I'll explain why. In the past, when the market produced the kind of explosive power-rise that we've just seen, that action has been the springboard for a further rise, and such rises often continue for a few months or more. Furthermore, the recent spurt came out of a ten-month sideways consolidation or "line" in the Dow. As a rule, a breakout from an extended line (either to the upside or the downside) will carry considerably further in the direction of the breakout.



But here's the fascinating part of it. The stock market was seriously OVERVALUED even before the upside breakout. So further upside action (if it occurs) would take the widely-followed averages (specifically the Dow and the S&P 500) into absolute "never-never land" -- the area of astronomical overvaluation.

To provide a better perspective, I'm including two charts (page 2). The first [courtesy of *Ned Davis Research* -- (800) 241-0621] shows the Dow price-to-dividend ratio. Put another way, the chart shows how many dollars it takes to buy one dollar of Dow dividends. Currently, it takes 35.70 dollars to



buy one dollar of Dow dividends. Only once before (see chart) has the Dow been valued this richly, and that was in August 1987 just before the huge 503-point crash.

This chart reveals more than simply the fact that the current Dow is extremely expensive. It traces the swings in market sentiment -- from enthusiasm (as seen today) down to abject pessimism and then back to enthusiasm again. Note that all periods of super-optimism have been followed by periods of severe pessimism and last area of pessimism occurred during the early '80s when the Dow could have been bought for as little as 14 times its dividends. Actually, this chart might better be called "a study in the madness of crowds," since it traces the path of market swings from one extreme of the emotional spectrum to the other.

Looking back over this chart, you have to ask yourself, "How could people be so pessimistic and wrong at the bottoms, and how could they be so enthusiastic and wrong at the tops?" Answer: it's human nature -- fear and greed are an integral part of human nature, and in the stock market emotions tend to go to extremes.

The second chart provides another way of looking at the same picture [courtesy of *Investment Quality Trends* -- (619) 459-3818]. Here we see the Dow going back to 1947 with four lines -- a line showing where the Dow would be at a yield of 3%, 4%, 5% and 6%. The 3% line represents the area of extreme overvaluation, the 6% line represents the area of severe undervaluation. The 4% and 5% lines represent stops between the two extremes.

This chart shows very dramatically how the Dow surged above the 3% valuation line during 1987, and it shows the same phenomenon occurring today. The chart also shows that the only other time (since World War II) that the Dow pushed above the 3% yield line was in 1966 just prior to the 1966-74 bear market.

The chart pinpoints the downside areas of great bargains just as clearly. All during 1947 to 1953 the Dow fluctuated around the 6% undervaluation area. Again in late-1974 the Dow sank into the area of undervaluation and bargains. And most recently, the Dow spent the majority of the period from 1977 to 1982 in the undervalued zone.

Since 1982 it's been up, up and away -- too far above overvaluation in 1987, and then came the crash. But note that even at the crash bottom in 1987 the Dow dropped only to the 4% yield zone, and that for a single month. Since the '87 low the Dow has plowed higher, and now for only the third time since World War II we find the Dow selling below even the 3% level of overvaluation.

Will it be different this time? Is valuation history in the process of being revised? My own opinion is that, no, nothing has changed. We're simply seeing human nature in action, and the market is now in its euphoric period, when, for whatever reason, investors are willing to buy the Dow at levels which, historically, have always been associated with major tops.

As a matter of reference, the Dow at a dividend yield of 3%, which is the overvalued zone, would sell at 3085. At a 4% yield the Dow would sell at 2314. At a 5% yield the Dow would sell at 1851. And at 6%, the bargain area and the area of major bear market bottoms, the Dow would sell at 1542 (Note: as mentioned, the Dow at 2.89% yield, is now selling above the price level of the overvalued zone).

My friend, Gerry Weiss, publisher of *IQ Trends*, puts the picture in perspective in her latest report,*"Our final words to the wise. Successful investing is a lifelong process. Some years are better than other years, and it is a mistake to denominate financial progress into 12-month periods. A lifetime of successful investing requires a lifetime to accomplish. The year ahead will be tough for investors. Interest rates are now low in the money market, so investors who bank on interest income may have to lower their living standards in 1992. Prices are high in the stock market and likely to decline; so, unless they are careful, investors who look for capital gains in the stock market will experience losses instead."*

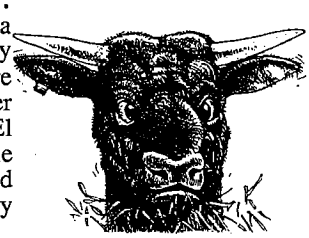
Gerry isn't talking through her hat -- she's talking from experience, and she's being guided by those chart lines. It all boils down to this -- you can identify the area where the stock market boiler has become seriously overheated, but nobody can pin-point the exact level at which intense heat will blow up the boiler.

COMMENTS: Is the stock market in its own world, dreaming of a recovery that isn't going to materialize? History tells us that the market tends to be right -- but yeah, there are always those dramatic exceptions. And that, of course, is what makes the study of markets and economics so fascinating. According to the latest *USA Today/CNN/Gallup* poll, 93% of Americans say that economics will be the top election issue. Furthermore, 71% of those polled state that the economy is getting worse, not better. The *NY Times* (Jan. 16) carried a feature article which states that the new sentiment in the US is towards "stinginess" and modest living. People are shying away from high-visibility spending and luxury living. It's now considered "in" to spend less, buy at discount stores, and act like a skinflint.

I think this new attitude is a reaction to today's layoffs and widespread unemployment. I think it's a reaction to the numerous "hard luck" and "down-and-out" stories featured in every issue of the daily newspapers. I also think the new attitude is a reaction, a turning-away, from the leveraged, free-spending, "sky's the limit" atmosphere of the 1980s.

Will this new conservative sentiment last? Obviously, there's no way of knowing. But if it does last, if it represents a basic reversal in attitude for the American people, then this will be the "big surprise of 1992" and maybe of 1993 and '94. And judging from current sky-high market valuations, neither Wall Street nor Washington is prepared for it.

INVESTMENT POSITION: With the yield on the Dow at a minuscule 2.83% (and historically dangerous) it probably makes more sense to put a pig in the box rather than a bull or bear. Nevertheless, El Toro owns the space, based on the upside breakout of the averages, and based on the new high in my Primary Trend Index.



But I've got to be honest. With today's wild valuations, I can't, in good conscience, tell my loyal subscribers to do what every other service and brokerage house is telling their followers to do -- and that's BUY, buy, buy. I do think that what we've seen is a Fed-manipulated collapse in interest rates, a collapse which drove money managers out of fixed income securities and into stocks. The rise fed on itself, and buyers lined up in a frantic race to gobble up as much equity as possible.

So please, study those charts on page 2. They go back a long way in history, and they tell a cautionary story. I believe in them. I suggest that you do the same.

READING: I've got five kids ranging from age 11 to 35. And this gives me a pretty good idea of what's going on with three generations (my generation, the 20 to 30 generation, and the current elementary and junior high generation). In view of that, I was particularly interested to read a recent interview with author Norman Mailer in *Time* magazine. Mailer is a keen observer. He's also ahead of me -- he has nine kids (so does Marlon Brando, who was born a month ahead of me, and who, I hear, has one more on the way courtesy of his ex-housekeeper).

When asked about his younger kids, Mailer said that they've been ruined by TV. I know exactly what he means. The first thing my two younger kids (11 and 14) want to do when they walk in the house is turn on the TV. And I'm worried that the tube is going to turn their little minds to mush (it's already hard to talk to them). Well, that's a slight exaggeration, but what TV really does is cut WAY DOWN on my kids' reading.

When I was a boy I was a voracious reader. I would read one book, and that book would excite me to read three other books. My problem was that I never had enough time to read all the books that were on my "must read" list. The reading habit has lasted me all my life, although today I spend more time reading newspapers and magazines than books (I read almost no fiction).

I'll admit it -- I have a love affair with reading. A huge percentage of what I've learned has come from reading. I've always felt that everything we need to know is there for us in books, magazines and newspapers. Walk into any library, and you're overwhelmed with a fantastic mountain of knowledge stacked shelf upon shelf. One of my frustrations is still that I haven't got time (actually, my eyes wouldn't hold out) to read all the books I'd like to -- books from "Peter the Great" to the latest Elmore Leonard novel to "War Planes of World War II."

So I worry about my kids and their obsession with TV. Watching TV is passive; reading books is active. That's the big difference. Watching TV means taking in what the broadcasters elect to give you. Reading entails you picking out what you want to read. I watch TV -- actually, I watch a lot of it, but I do it mostly for relaxation. I'll never believe that TV takes the place of reading. I wish my younger kids felt that way. Maybe someday they will -- or has TV already captured (seduced) their impressionable minds?

A recent study by the American Booksellers Assoc. comes out with the shocking news that 60% of US households didn't buy a single book last year. They also stated that the largest group of bookbuyers are senior citizens. The Nov. 18 issue of *Fortune* magazine headlined an article, "America Won't Win Till It Reads More." I believe it. *Fortune* quotes Monsanto CEO Richard Mahoney, as follows: "People who read more seem to have that marvelous ability to see linkages between unrelated events. That's the most important quality an executive can have." *Fortune* adds, "Research backs up Mahoney's point: In general, the higher a person's reading skills, the higher his professional achievement." I firmly believe that too.

NOTES & QUOTES: How bad is it in the recession-wracked state of New Hampshire? Last week Dime Savings Bank of NY was foreclosing on the home of Chris Spirou, the Democratic state chairman. Said Spirou, "I am without doubt a victim of the Reagan-Bush demolition derby." You're up, George.

* *

The reaction to Bush's jaunt to Japan was amazing. The trip seemed to release all the pent-up distrust, anger and disgust which has been building against the Bush administration. Even Bush's foreign policy, supposedly his forte, has come under fire. A.M. Rosenthal (*NY Times*, Jan.10) includes a long list of Bush errors and disasters: (1) Bush allowed Saddam to remain in power. (2) Bush sat back and allowed Saddam to practice genocide against the Kurds. (3) Bush stubbornly backed Gorbachev, wrongly thinking Gorby could hold the Soviet empire together. (4) Bush reneged on US pledge to support Baltic independence. (5) In Kiev Bush lectured on dangers of independence for Soviet satellites (when that's all the satellites wanted). (6) Bush sat on his hands while leadership of Europe went to Germany. (7) Bush is still the main supporter of Syria and its dictator, despite the fact that Syria is almost identical to pre-war Iraq. (8) Bush still clings to his peculiar taste for the Chinese Communist leaders. (9) Bush led disastrous sales pitch to Japan and came across as an unsuccessful car salesman.

Doug Bandow in another *Times* piece wrote (Jan 12), "Especially damaging is the continued support by Bush ('Read my lips') for a budget deal that has simultaneously given us the largest tax hike in history, the fastest domestic spending increases since the New Deal, and the largest budget deficits in history . . . At first Bush didn't recognize his own recession, then he thought that ignoring it would make it go away . . . And now he desperately casts about for answers, pushing down interest rates (which hurts savers), calling a bloated, wasteful transportation bill a jobs bill, taking executives who can't sell in America to Japan (which showcases American incompetence), and coming up with a few little fixes that leave the economy's fundamental weaknesses unattended. 'Wait for my State of the Union Speech', Bush says."

But the most damning piece was written by Leslie Gelb (*NY Times* --Jan. 13). "The Bush mission to Japan was so ill conceived and executed as to raise fundamental doubts about the President's capacity to manage US foreign policy in the post-cold war world. Bush doesn't understand that international power now depends on domestic economic strength. And so he went to Japan in the worst possible way-- to bash on bended knee . . . Neither he nor his closest advisors know the first thing about Japan, perhaps the country that will have the most profound impact on US interests. In their ignorance, they unleashed an attitude that could have the direst consequences . . . Power in this world turns on internal economic strength. By that measure, the US is in relative decline -- on education, infrastructure, the running of many traditional industries and self-discipline. Mr. Bush seems to perceive this central fact only dimly. Bush hitched his and America's prestige to the big three auto whiners who, along with Mr. Bush, had to be among the select few who were blind to the looming catastrophe. The whiners are the guys who pay themselves more than 100 times their workers' salaries or 10 times higher than their Japanese counterparts; who raise their compensations even as their companies' profits plummet, and who cry about not being able to sell cars in Japan when the Japanese drive from the right side."

Russell comment: Bush's approval rating, at a high of 89% after the war, has now dropped to a critical 46%. I think the collapse in ratings is warranted. My own feeling is that I've seen enough of Bush -- he doesn't understand the new international economics, I feel he's intellectually dishonest, and his obsession with getting re-elected at all costs disgusts me.

* *

An article, "A Paranoid's Guide to Tax Increases" in the current issue of *Forbes* (Jan. 20) is MUST reading. Gist of the piece -- taxes are heading up, and if you have big bucks, maybe the best thing to do is "spend while you are young" and "give away as much as you can to your heirs before you die. If the worst comes to the worst, the taxpayers will take care of you." This eye-opening article gives reasons why you should "be leery of salary deferment plans," why you "should not buy a vacation home," why "if you buy bonds you should buy municipals," why you "should not live in a high-tax state," why you should "give away assets to your heirs," and why "you should take small capital losses now." The article is based on the thesis that over the long run, inflation will rule, and the government will tax us to death. Russell comment: inflation, over-spending, deficits and higher taxes -- that's been the history of the US; why shoot, they're all as American as apple pie. (Note: According to the National Conference of State Legislatures, more than half the states will need to raise taxes, cut spending or raid reserve funds to balance their budgets this fiscal year.)

Meanwhile, who suffers? Well, we all do, and so does the purchasing power of the good ol' dollar. When a currency's

purchasing power collapses, it means that the savers are wiped out. That's exactly what's been happening. For instance, I still have my $10,000 GI life insurance policy, issued during WWII. At the time, the policy seemed like an important safety cushion. Today? It's a bad joke.

* *

With the the collapse of the Soviet empire and a democratic Germany and Japan, the chances of World War III are now literally non-existent. The military struggle for world supremacy has ended, but the economic battle is now on -- full force. The coming growth area will be Asia, and, in fact, the battle for economic supremacy in Asia is already well underway. The model for capitalism in Asia is not America's consumer-driven style of capitalism, it is Japan's disciplined bureaucracy, long-view economic planning and tradition of partnership between government and private business. Says Asian specialist (UCSD) Professor Chalmers Johnson, "The most important fact in the post Cold War Asia-Pacific region is Japan's growing economic dominance, and the degree to which it is integrating the region through trade, direct investment aid, financial services, technology transfer and a continuing role as a developmental model." Writes *US News & World Report* (Jan. 6), "The showdown within capitalism is reaching beyond Asia. Mexico has dispatched specialists to study Seoul's booming economy, which is roughly patterned on Tokyo's model . . . Malaysian Prime Minister Mahathir says bluntly that his nation intends to become an industrial power by emulating Japan, not America. He has proposed an Asian bloc that includes Japan but that would exclude the US, Canada and Australia."

You can see the tremendous pressure building to shrink the US military. It is coming from the need to pump money into the rest of the US economy, and as the recession lingers on, as the demand for government spending increases, and as the realization that the US no longer has any major enemies, I look for a steadily contracting US military. But maybe the biggest pressure on the military stems from this fact -- after spending billions of dollars, francs and pounds on weaponry and manpower, military power is no longer the measure of a nation's strength. Look at the collapse of the Soviets, look at the declining US power after Vietnam and Panama and Granada and Iraq. And look at the growing power of non-military Germany and Japan.

* *

Interesting fact: it cost $7.3 million a year just to service and keep one B-4 bomber going. News: Bush announces that the US will save $25 billion by cutting the planned total of 75 B-2 Stealth Bombers down to only 20. One result -- it will be a blow to S. California where Northrup has 13,000 people assigned to the B-2.

* *

Ross Perot (CEO of Perot Systems Inc. and former head of Electronic Data Systems) is talking: "Let's have a US version of Japan's MITI . . . to create long-term plans for important industries of today and tomorrow. We are going to do what the Japanese do, support our important industries. They have had every important industry and company in our country under a microscope. And they use that intelligence to achieve their own national ends. Contrast that to our country where there is an adversarial relationship between government and business. We need a planned, organized program to build industry." Perot wants a series of meetings between Congress and the White House: "They should work together night and day to put our country back on track . . . announce that the country is more important than the 1992 election and pledge to stay away from plans that will temporarily ease the pain for Americans so that the politicians can get elected. Third, pass a new law that federal spending cannot exceed the government's income. Fourth, stop pandering to special interest lobbyists, especially foreign governments. Get rid of the perks in Washington. Get rid of the airplanes owned by the government and used to fly people around. Get rid of the five florists in the White House. Agree to stop doing things simply to get TV time. Why should the President take all these businessmen around the world with him? If those businessmen worked for me, I'd say, 'Listen suckers. We got problems. Don't be wandering around the world going to parties and receptions with the President. Let's get out in the field and fix our problems.' This trip is nothing more than an election year media stunt." Russell comment: One of these years, when things get bad enough, this nation will elect a man like Perot for president.

* *

The 1992 election could hinge on California. If Bush loses California, he will be the first Republican presidential candidate to lose the state since Barry Goldwater in 1964. The Golden State has 52 House seats, and California now holds 20% of the electoral votes needed to win. The Dems, who are now weak in the South, also need California in order to win. Should be interesting.

* *

Statistics: One in every five Americans was unemployed at some point last year . . . One out of 10 Americans received food stamps this year . . . One in every 53 New Yorkers is infected with the HIV virus . . . California prison budget is $2.5 billion a year . . . US car makers did badly last year, but for Europe's car makers it was a disaster. Mercedes' US sales dropped 25%, Jaguar dropped 50% and Porsche fell 52%. VW was down 29% and total sales of VWs fell below 100,000 for the first time since 1959 . . . In 1990 the American standard of living dropped by the greatest amount since 1947. By the end of 1992, family income in the US will have dipped below the 1989 levels . . . Today 80% of those employed in the US are in service industries . . . Over 200,000 white collar jobs have been lost in this recession so far. During the recessions of 1973-74 and 1981-82 white collar jobs increased by an average of 800,000.

* *

You really want to know what's going on in the world? Then read the *Economist* and the *International Herald Tribune*. This from last week's *Tribune:* "With most of Western Europe in or near recession and much of Eastern Europe in disarray, the Continent has rarely been in greater need of the fabled German economic locomotive to pull it out of trouble. Unfortunately, Germany itself is hovering on the edge of recession, business confidence is sliding and many analysts say the economy is in its most fragile condition in a decade . . . And all at a time when the grand experiment of converting Eastern Germany to capitalism looks set to drain resources for years." Russell comment: Germany now has to deal with 20,000 East Germans migrating to the West every month, and that is one huge strain.

* *

I've been fantasizing about the coming election. None of the Democrat candidates have any great stature or national voter-following. So why not run all five of them as a unit against Bush? If the Dems win (and five against one might win), let them draw lots, with the winner becoming our new president. Then the new Democrat president could pick Bush for the job which he's really been working at all along -- Secretary of State. I mean, is this a stroke of genius or what! One of the humor mags suggests Duke for president and Jesse Jackson for vice-president, but nah, I don't think that would work.

* *

Older Investors Reel at Brink of Plunging Rates

■ **Savings:** Although rock-bottom interest rates benefit home buyers, they hurt retirees' investments.

By DENISE GELLENE
TIMES STAFF WRITER

Back in the early 1980s, with interest rates in the stratosphere, Raymond Spivak looked forward to a carefree retirement on money saved during his 40 years as a garment salesman. In those days, money Spivak deposited in the bank was earning a lofty 15%.

Today, with rates at their lowest level in 28 years, the now-retired Spivak has found that he can no longer afford his comfort-

The over-60 population are the savers, and they also have big buying-power capabilities. Many of these oldies are living off of Social Security plus interest on their savings. The plunge in interest rates has decimated their buying power (interest-income is the key to their discretionary spending). Since consumer spending constitutes two-thirds of GDP, today's lower interest rates may hurt the economy as much as help it.

NOTE: I continue to offer two important looseleaf (three ring) **chart albums.** The first covers the the **daily D-J Averages** (Industrials, Transports, Utilities, Bonds and Volume) going back to 1885, one page for each year. There are numerous notations of important news events on each page so that students can see how the market reacted to the events of the day. The price for this album (postpaid -- please add US$35 for foreign air parcel post) is $135. This album is unique, nobody else does it, and it's an invaluable tool for every market student and investor.

I also offer a similar looseleaf album of the **Dow and the Advance-decline ratio** daily going back to 1931. The price for this album is $95 postpaid (please add US$35 for foreign air parcel post). I urge all serious market students to buy these albums. Personally, I would not be without them (originally, I produced these two albums because I needed the charts and data myself and there was no other place to find them). **NOTE:** The new 1991 pages for both albums will be ready in February, price per page is $3. Please send in your orders now.

METALS & MUSINGS: The question going through everyone's mind is this -- "Is the stock market truly forecasting an end to the recession, or has the 20-year low in interest rates panicked the institutions and the saving-public, sending them helter-skelter into the stock market, forcing them to buy 'any stocks at any price'?"

At this point we don't know the answer, and as a result, economists, analysts and market students are hanging on every tid-bit of news, every corporate announcement, every (mostly mindless) rumor out of Washington.

My old friend Joe Granville has always (at least since 1961, when I first started trading letters with him) stated that the news of the day has little or nothing to do with the path of the stock market. Joe adds that it's only the market's REACTION to the news that is significant. And Joe is largely right.

It is said that earnings move the market, but this is true at times, and at other times it is not. The big mover in the market is sentiment, price/earnings, or what people are willing to pay for earnings. Back in 1974 when the Dow was below 600 people were very (wrongly) pessimistic and they were willing to pay only 6 or 7 times earnings for the Dow. Of course, that made the Dow a fantastic bargain. Today, people are extremely optimistic, and they are rushing to pay 32 times the Dow's earnings. Are they right today, or will history prove them to be as wrong as they were back in 1974? Only time will tell, but the charts on page 2 suggest that they will be wrong.

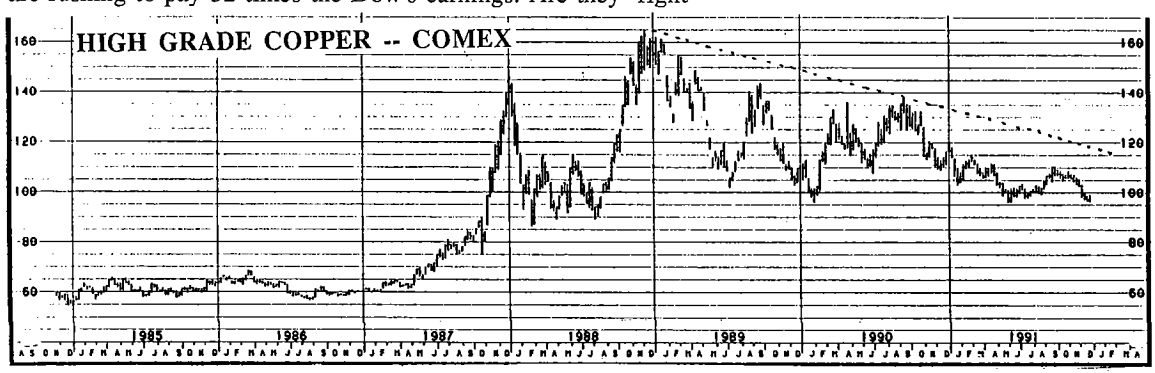
Incidentally, I just received the latest issue of *IQ Trends,* and their Percentage of Undervalued Blue Chip Stocks has now dropped to 8%, the lowest percentage since they started these tabulations back in the '60s. Thus, one can make a good case for this being the most overvalued stock market probably since World War II (at the 1966 market top the percentage was 10%, at the '73 top it was 17%, at the '87 pre-crash top it was 12%; we've never seen a figure as low as 8%).

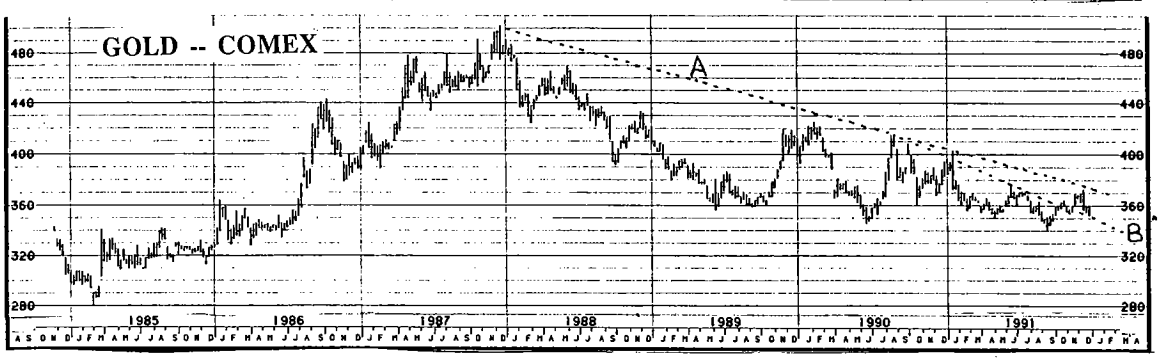
Here are two long-term charts (courtesy of *Commodity Research Bureau*) that are worth studying. The first is copper, which over the years has been a good barometer of forthcoming economic activity (almost all industries use some copper in whatever they're doing). In the past, when the economy was rising, copper headed well over a dollar a pound, often climbing over 1.40. Currently, copper is below one buck. If the US economy is going to revive, we should see it in the trend of copper. Not much action here yet.

The second chart traces gold going back to '85. Gold rallied to the end of 1987, at which point it topped out and so did inflation. Since '87, gold has headed down (trendline A), although it found support in the 345-350 area. A second trendline (B on chart) connected a 1990 and two '91 tops. The B trendline was recently penetrated to the upside. The significant upside target for gold is the preceding peak at 375. If gold betters 375, I would say that the trend has definitely turned up.

Meanwhile, a gold stock (oft recommended here) that seemingly can't wait to go higher is American Barrick (NYSE). Last week ABX hit a new high of 29. I still like it.

LATE NOTES: As of January 17 almost all averages and indices were in gear on the upside -- with the single exception of the Utilities. The D-J Industrials and Transports were at record highs (page 1 chart) and the A-D ratio and my PTI were also at new highs (the PTI was at a record high of 3445). What about the lagging Utility Average? This Average posted its high on December 31 at 226.15, and it has since declined to the 211 area. The Utilities often lead the rest of the market, but that lead can be a matter of many months. Why a decline in Utilities? One theory is that investors are moving out of the relatively "stodgy" Utility stocks into more venturesome areas. A second theory is that the Utilities are telling us that the bottom for interest rates has been seen, and that rates (particularly long rates) are in the process of creeping up again.





In the meantime, the operative phrase on Wall Street is "Buy 'em". Cautionary signals, based on historic value measurements, have been jettisoned like so much rotten baggage. And that 8% figure on Undervalued Blue Chip Stocks keeps coming back to haunt me.

Next Letter Feb. 5.

See you then. In the meantime, keep your eye -- on the Nikkei.